MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

2010 ANNUAL REPORT

LETTER OF TRANSMITTAL

Regina, Saskatchewan
March 15, 2011

To His Honour
The Honourable Gordon Barnhart
Lieutenant Governor of the Province of Saskatchewan

Sir:

I have the honour to submit herewith the Annual Report of the Municipal Financing Corporation of Saskatchewan for the year ended December 31, 2010, in accordance with **The Municipal Financing Corporation Act.** The financial statements included in this Annual Report are in the form approved by the Treasury Board and have been reported on by the Corporation's auditors.

I have the honour to be, Sir,

Your obedient servant,

/s/ Ken Krawetz

Ken Krawetz
Minister of Finance
And Minister Responsible
Municipal Financing Corporation of Saskatchewan

MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

BOARD OF DIRECTORS

Honourable Ken Krawetz
Chairperson

Honourable Darryl Hickie

OFFICERS

Rae Haverstock
General Manager

Denise Macza
Assistant General Manager

Jim Fallows
Treasurer

Emily Guo
Secretary

CONTACT INFORMATION

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MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

HISTORY AND CURRENT HIGHLIGHTS – 2010

The Municipal Financing Corporation of Saskatchewan (the Corporation) was established to assist in making capital funds available for the financing of school, hospital and other essential construction and local improvement projects in cities, towns, villages and rural areas throughout the Province. The Corporation may borrow directly from private lending institutions or through the Ministry of Finance. The Corporation uses the funds borrowed to purchase a portion of the approved debentures sold each year by Saskatchewan local governments.

The Corporation participated in the financing of 9 projects by purchasing $5.0 million of debentures. Most of the debentures financed sewer and water projects or land development projects.

The Corporation's debenture holdings at December 31, 2010 totaled $110.7 million, up $0.9 million from the total at December 31, 2009.

The Corporation recorded net earnings of $1.4 million in 2010, which exceeds the surplus of $1.2 million recorded in 2009 and the $1.3 million amount budgeted (see note 9 to the financial statements). The increase in net earnings is attributable to growth in the size of the Corporation's loan portfolio and higher than anticipated earnings on sinking fund investments.

For 2011, the Corporation expects net earnings to be slightly lower than the amount recorded in 2010 due to additional interest expense on the Corporation's debt.

The Municipal Financing Corporation of Saskatchewan is administered by a Board of Directors through the use of staff and facilities provided by the Ministry of Finance. The Corporation incurred $25,000 of administrative expenses in 2010. These expenses were primarily for audit fees and the reimbursement of the costs to the Ministry of Finance of providing administrative services. The Directors of the Municipal Financing Corporation of Saskatchewan do not receive fees and, with the exception of interest paid on borrowed funds, the Corporation had no other expenses in the current year.

A table showing results of operations for 2010, as compared to the previous year, as well as a detailed listing of debentures purchased in the current year is presented on page 4.

MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

COMPARATIVE TABLE OF OPERATIONS
FOR THE YEAR ENDED DECEMBER 31

	2010	2009
	(thousands of dollars)	
Amount of debentures offered to the Corporation	$ 4,976	$ 62,574
Prior year's purchase commitments carried forward	0	2,000
Total purchase commitments for the year	4,976	64,574
Purchases completed	4,976	64,574
Purchase commitments outstanding at the year end	$ 0	$ 0

DEBENTURES PURCHASED IN 2010
(thousands of dollars)

Town of Biggar	$ 623
Town of Carlyle	1,000
Town of Cudworth	300
Town of Rose Valley	254
Town of Sturgis	1,394
Town of Wapella	415
Village of Buchanan	400
Village of Kenaston	175
Village of Viscount	415
	$ 4,976

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

Management has prepared the financial statements of the Municipal Financing Corporation of Saskatchewan in accordance with Canadian generally accepted accounting principles applied on a basis consistent with that of the previous year. Management is responsible for the reliability and integrity of the financial statements and all other information contained in this Annual Report.

Management has the primary responsibility for the integrity and objectivity of the financial statements. To fulfill this responsibility, management maintains appropriate systems of internal controls, policies and procedures to provide reasonable assurance that assets are safeguarded and that the books and records reflect the authorized transactions of the Corporation.

Dudley and Company LLP, the Corporation's external auditors, have reviewed the systems of internal control and audited the financial statements in accordance with Canadian generally accepted auditing standards to enable them to express their opinion on the financial statements. Their report appears on the following page.

The financial statements have been examined and approved by the Board of Directors.

/s/ Rae Haverstock

Rae Haverstock
General Manager

/s/ Jim Fallows

Jim Fallows, CA
Treasurer

March 15, 2011

INDEPENDENT AUDITOR'S REPORT

To the Members of the Legislative Assembly, Province of Saskatchewan

We have audited the accompanying financial statements of the **MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN** which comprise the statement of financial position as at December 31, 2010 and the statements of earnings and reinvested earnings and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the **MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN** as at December 31, 2010, and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

/s/ Dudley & Company LLP

Dudley & Company
Chartered Accountants LLP

Regina, Saskatchewan
March 15, 2011

MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

STATEMENT OF FINANCIAL POSITION

As at December 31

	2010	2009
	(thousands of dollars)	
ASSETS		
Current assets		
Due from General Revenue Fund (Note 3)	$ 1	$ 85
Interest receivable	1,395	1,365
Municipal debentures receivable within one year	4,395	4,068
	5,791	5,518
Investments in municipal debentures (Note 4)	106,314	105,732
Deferred financing charges	42	53
	$ 112,147	$ 111,303
LIABILITIES AND PROVINCE'S EQUITY		
Current liabilities		
Interest payable and accrued liabilities	$ 588	$ 489
Debt payable within one year (Note 6)	5,299	15,656
	5,887	16,145
Long term debt payable (Note 6)	89,752	80,009
Province of Saskatchewan's Equity		
Reinvested earnings	16,508	15,149
	$ 112,147	$ 111,303

(See accompanying notes)

MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

STATEMENT OF EARNINGS AND REINVESTED EARNINGS

For the Year Ended December 31

	2010	2009
	(thousands of dollars)	
Revenue		
Investment income - municipal debentures	$ 4,661	$ 3,672
Investment income - short term investments, sinking funds and cash balances	102	35
	4,763	3,707
Expenses		
Interest on debt	3,379	2,529
Administration	25	27
	3,404	2,556
Net Earnings	1,359	1,151
Reinvested earnings, beginning of year	15,149	13,998
Reinvested earnings, end of year	$ 16,508	$ 15,149

(See accompanying notes)

MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

STATEMENT OF CASH FLOWS

For the Year Ended December 31

	2010	2009
	(thousands of dollars)	
Operating Activities		
Interest received from municipal debentures	$ 4,641	$ 3,455
Interest received from short term investments	1	8
Interest paid on debt	(3,278)	(2,472)
Payments to suppliers	(25)	(27)
Cash provided by operating activities	1,339	964
Investing Activities		
Purchase of municipal debentures	(4,976)	(64,574)
Proceeds from maturing municipal debentures	4,068	3,625
Cash used in investing activities	(908)	(60,949)
Financing Activities		
Issuance of short term debt	0	15,656
Repayment of short term debt	(10,357)	0
Issuance of long term debt	10,174	43,100
Repayment of long term debt	(332)	(332)
Cash provided by financing activities	(515)	58,424
Net (decrease) in cash equivalents during the year	(84)	(1,561)
Cash equivalents, beginning of year	85	1,646
Cash equivalents, end of year	$ 1	$ 85

(See accompanying notes)

MUNICIPAL FINANCING CORPORATION OF SASKATCHEWAN

NOTES TO FINANCIAL STATEMENTS

December 31, 2010

1. Significant Accounting Policies

Pursuant to standards established by the Public Sector Accounting Board, the Corporation is classified as a government business enterprise. These financial statements are prepared in accordance with Canadian generally accepted accounting principles applicable to for-profit entities.

Financial Instruments

The Corporation has implemented the following classifications:

- Short term investments are classified as "financial assets held for trading," so they are marked to market through net income at each period end. For the Corporation, the measured amount generally approximates the cost.
- Due from the General Revenue Fund and Interest receivable are classified as "loans and receivables." After initial fair value measurement, they are measured at amortized cost using the effective interest rate method. For the Corporation, the measured amounts generally approximate their cost.
- Municipal debentures receivable within one year and investments in municipal debentures are classified as "held to maturity investments." After initial fair value measurement, they are measured at amortized cost using the effective interest rate method.
- Interest payable and accrued liabilities, debt payable within one year and long term debt payable are classified as "other financial liabilities." After initial fair value measurement, they are measured at amortized cost using the effective interest rate method.
- Sinking funds are classified as "financial assets held for trading," so they are marked to market through net income at each period end. Sinking fund assets are netted against long term debt payable because the Corporation has a legally enforceable right to set off the amounts and intends to realize the asset and settle the liability simultaneously.

Comprehensive Income

The Corporation does not have any comprehensive income and accordingly, it has not presented statements of other comprehensive income and accumulated other comprehensive income.

Deferred Financing Charges

Deferred financing charges relate to long term debt payable and are amortized over the term of the related debt.

Future Accounting Changes

In February 2008, the Canadian Accounting Standards Board confirmed that publicly accountable enterprises, including the Corporation, will be required to adopt International Financial Reporting Standards (IFRS) in place of Canadian GAAP for interim and annual reporting in fiscal years beginning on or after January 1, 2011, including comparative figures for the prior year.

The impact on the Corporation's future financial statements is not expected to be significant.

2. Status of the Corporation

The Municipal Financing Corporation of Saskatchewan was established in 1969 pursuant to the provisions of **The Municipal Financing Corporation Act**. The Corporation's objective is to assist municipalities in financing their capital requirements.

The Corporation is a Provincial Crown corporation and is therefore not subject to Federal or Provincial income tax but is subject to Provincial corporation capital tax.

3. Due from General Revenue Fund

The Corporation's bank account is included in the Consolidated Offset Bank Concentration arrangement for the Government of Saskatchewan.

The Corporation's earned interest is calculated and paid quarterly by the General Revenue Fund to the Corporation using the General Revenue Fund's thirty day borrowing rate and the Corporation's average daily bank account balance.

4. Investments in Municipal Debentures

The Corporation invests in fixed rate debentures issued by cities, towns, villages, rural municipalities and school divisions throughout the Province of Saskatchewan. Debentures purchased by the Corporation must be approved by the Saskatchewan Municipal Board, where applicable.

The Corporation has an investment in 107 (2009 - 105) debentures issued by 74 (2009 - 72) issuers with a weighted average yield of 4.19% (2009 – 4.23%) and maturity dates ranging from 2011 through 2030.

The carrying amount invested by issuer category is as follows:

	2010	2009
	(thousands of dollars)	
Cities	$ 69,021	$ 69,749
Rural Municipalities	892	951
Towns	27,305	25,701
Villages	6,451	6,079
School Divisions	7,040	7,320
	110,709	109,800
Receivable within one year	4,395	4,068
	$ 106,314	$ 105,732

The fair value of these debentures is $116.9 million (2009 - $116.7 million). This fair value is determined by discounting the debentures' future cash flows using investment rates presently available to the Corporation for investments with similar terms and remaining maturity. Prepayment rates and credit losses are assumed to be zero, based on the past experience of the Corporation. A one per cent change in the investment rates noted above would change the fair value of these debentures by approximately $4.6 million. The Corporation measures its investments in municipal debentures at amortized cost using the effective interest method, so a change in the fair value of these securities would have no immediate effect on net earnings.

The Corporation's policy is to permit borrowers to redeem debentures prior to maturity. Effective March 2009, the redemption price is set at the fair market value of the debenture. Prior to March 2009, the redemption price was set at the face value of the debenture plus 50% of the difference between the face value of the debenture and its fair market value. During 2010 and 2009, no debentures were redeemed.

5. Related Party Transactions

Included in these financial statements are transactions with various Saskatchewan Crown corporations, ministries, agencies, boards and commissions related to the Corporation by virtue of common control by the Government of Saskatchewan. Routine operating transactions with related parties are settled at prevailing market prices under normal trade terms. These transactions are as follows:

	2010	2009
	(thousands of dollars)	
Interest on debt	$ 3,379	$ 2,529
Administration	20	20

Other amounts due from and to related parties and the terms of settlement are described separately in the financial statements and the notes thereto.

6. Debt

Maturity Date	Rate (%)	2010	2009
		(thousands of dollars)	
General Revenue Fund (GRF)			
June 17, 2013	4.75	$ 5,000	$ 5,000
December 1, 2013	3.80	4,800	4,800
June 5, 2014	3.11	43,100	43,100
March 1, 2015	2.93	10,174	-
December 3, 2015	4.25	5,000	5,000
April 10, 2017	4.41	2,800	2,800
December 1, 2018	4.74	7,000	7,000
June 10, 2022	4.81	3,900	3,900
August 8, 2026	4.86	7,330	7,330
April 10, 2027	4.60	2,200	2,200
		91,304	81,130
Less: sinking fund balance		(1,552)	(1,121)
Long term debt		$ 89,752	$ 80,009

The fair value of long term debt is $95.5 million (2009 - $85.3 million). This amount is determined by discounting the debentures' future cash flows using borrowing rates presently available to the Corporation for debt with similar terms and remaining maturity. A one per cent change in the borrowing rates noted above would change the fair value of long term debt by approximately $3.9 million. The Corporation measures its long term debt at amortized cost using the effective interest method, so a change in the fair value of long term debt would have no immediate effect on net earnings.

The sinking fund balance is reported at its fair value.

a) sinking funds

Under conditions attached to debentures with a term of ten years or more, the Corporation is required to pay annually into sinking funds administered by the Saskatchewan Ministry of Finance a minimum of one per cent of the original principal.

b) principal repayments and sinking fund installments

Principal repayments and sinking fund installments for the next five years are as follows (in thousands of dollars):

Year	Sinking Fund Installments	Principal Repayments	Total
2011	332	0	332
2012	332	0	332
2013	332	9,800	10,132
2014	282	43,100	43,382
2015	282	15,174	15,456

c) short term debt

The corporation sometimes borrows funds on a short term basis from the GRF. At December 31, 2010, an amount of $5,299 thousand was due to GRF at an interest rate of 1.13%.

7. Financial Instruments

Management of Financial Risks

The activities of the Corporation result in exposure to three types of risk:

i) Interest Rate Risk

Interest rate risk is risk that the value of the Corporation's assets and liabilities will fluctuate due to changes in market interest rates. This risk exists because the maturity dates of the Corporation's assets and liabilities are not precisely matched:

Year of Maturity	Financial Assets	Financial Liabilities	Difference 2010	Difference 2009
		(thousands of dollars)		
2010	$ -	$ -	$ -	$ (10,627)
2011	5,791	5,887	(96)	-
2 - 5 years	81,467	67,292	14,175	28,002
Thereafter	24,889	22,460	2,429	(2,226)
	$ 112,147	$ 95,639	$ 16,508	$ 15,149

The Corporation manages this risk by matching the maturity dates of material assets and liabilities to the extent possible.

ii) Liquidity Risk

Liquidity risk is the risk that financial obligations will not be met over the short-term due to lack of access to capital. This risk is managed by distributing debt maturities over many years, maintaining sinking funds on long-term debt issues and maintaining adequate cash reserves and an $80 million short-term line of credit with the General Revenue Fund.

iii) Credit Risk

Credit risk is the risk that the Corporation will not receive payment in full for its investments in municipal debentures or its investment in sinking funds.

For municipal debentures, this risk is managed by legislative restrictions on the amount that can be borrowed by a municipality and scrutiny of all proposed transactions. Few of the Corporation's municipal debentures have a credit rating, however all are considered secure. At December 31, 2010, the Corporation had a maximum exposure of $110.7 million (2009 - $109.8 million) on its investments in municipal debentures.

For sinking funds, this risk is managed by holding a diversified portfolio of investment grade fixed income securities. The investment guidelines applicable to the sinking funds prohibit the acquisition of non-investment grade securities. At December 31, 2010, the Corporation had a maximum exposure of $1.6 million (2009 - $1.1 million) on its sinking fund investments.

The Corporation has never experienced a credit-related loss.

Fair Value Information Regarding Financial Instruments

Fair value is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable, willing parties who are under no compulsion to act. The Corporation has classified the fair valuation of its financial instruments as level 1, 2 or 3 as defined below.

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The Corporation's sinking fund investments have been grouped into Level 2 of the fair value hierarchy. The sinking funds are valued by the Ministry of Finance using information provided by investment dealers. To the extent possible, valuations reflect indicative secondary pricing for these securities. In all other circumstances, valuations are determined with reference to similar actively traded instruments.

Other Information Regarding Financial Instruments

The effective interest rates on the Corporation's interest bearing financial instruments are as follows:

Investments in municipal debentures	4.19%
Long term debt	3.70%

The Corporation's financial instruments have the following carrying amounts:

	2010	2009
Financial assets held for trading	$ 1,552	$ 1,121
Held to maturity investments	110,709	109,800
Loans and receivables	1,396	1,450
Other financial liabilities	(97,191)	(97,275)
Net carrying value of financial instruments	$ 16,466	$ 15,096

The Corporation incurred gains of $44 (2009 – $20) on its financial instruments held for trading.

Total interest income on financial assets not held for trading was $4,661 (2009 - $3,672).
Total interest expense on financial liabilities not held for trading was $3,379 (2009 - $2,529).

The Corporation had no fee income or expenses arising from financial instruments not held for trading.

The Corporation had no impaired financial instruments, so no interest income or losses were incurred from such assets.

8. Capital Management

The Corporation defines its capital as its reinvested earnings and its long term debt payable.

The Corporation strives to ensure that the interest rate on its investment in municipal debentures exceeds the effective interest rate on its long term debt. The Corporation also attempts to match the payments required to service its long term debt to the cash flows expected from its investments.

The Corporation is not subject to any external or statutory capital requirements.

The points noted above have not changed from the previous fiscal year.

Information on the specific management of financial risks is included in Note 7.

9. Operations Budget

	Budget 2010
	(thousands of dollars)
Revenue	
Investment income - municipal debentures	$ 4,960
Investment income - short term investments and cash balances	40
	5,000
Expenses	
Interest on debt	3,670
Administration - Ministry of Finance	20
- Audit	5
- Other	5
	3,700
Net earnings	$ 1,300